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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of California-American Water Company (U210W) for Approval of the Monterey Peninsula Water Supply Project and Authorization to Recover All Present and Future Costs in Rates.

Application 12-04-019
(Filed April 23, 2012)

**ASSIGNED COMMISSIONER RULING, JOINED BY A CO-ASSIGNED
ADMINISTRATIVE LAW JUDGE, REQUESTING COMMENTS
ON SURCHARGE OPTIONS AND PROPOSALS**

1. Summary

This Assigned Commissioner Ruling, joined by a co-assigned Administrative Law Judge, requests comments of the Parties by May 12, 2014, and reply comments by May 16, 2014, concerning a specific surcharge proposal prepared by the Division of Water and Audits that is set out in this ruling at Appendix 1. The proposal would have Surcharge 2 set at 15% starting July 1, 2014, 30% when Surcharge 1 expires (estimated to be by November 1, 2014), and 45% on January , 2015, where it would remain until the desal plant is put into service.

2. Discussion¹

2.1. Settlement Agreement

¹ Portions of this ruling rely heavily on language contained in filings of the parties and documents prepared by the Division of Water and Audits (DWA).

On July 31, 2013, the following was executed: Settlement Agreement of California-American Water Company, Citizens for Public Water, City of Pacific Grove, Coalition of Peninsula Businesses, County of Monterey, Division of Ratepayer Advocates, LandWatch Monterey County, Monterey County Farm Bureau, Monterey County WaterResources Agency, Monterey Peninsula Regional Water Authority, Monterey Peninsula Water Management District, Monterey Regional Water Pollution Control Agency, Planning and Conservation League Foundation, Salinas Valley Water Coalition, Sierra Club, and Surfrider Foundation (Settlement Agreement). It is “Attachment A” to the *Settling Parties’ Motion to Approve Settlement Agreement*, filed in Application 12-04-019 on July 31, 2013. All parties to the Settlement Agreement have signed onto in this Joint Motion except LandWatch Monterey County, Monterey County Farm Bureau, Monterey Regional Water Pollution Control Agency, Salinas Valley Water Coalition, Sierra Club, and Surfrider Foundation, who stated they are not joining in this motion because it goes beyond the scope of their involvement in the proceeding.

2.2. Surcharge Background

See Appendix 3.

2.3. Joint Motion and Its Denial

On March 14, 2014, California-American Water Company (Cal Am), Citizens for Public Water, City of Pacific Grove, Coalition of Peninsula Businesses, County of Monterey, Monterey County Water Resources Agency, Monterey Peninsula Regional Water Authority, Monterey Peninsula Water Management District, the Office of Ratepayer Advocates, and Planning and Conservation League Foundation filed a Joint Motion to Reduce the Special Request I Surcharge. Assigned Administrative Law Judge (ALJ) Weatherford

denied that motion without prejudice by an e-mail ruling² on March 20, 2014, stating:

The Joint Motion filed on Friday March 14, 2014, seeking a reduction in Surcharge I, is denied without prejudice. I will be consulting with staff concerning ratepayer impacts and surcharge mechanisms generally and longer term relative to this proceeding.

2.4. Division of Water and Audits Options and Proposals

After ALJ Weatherford conferred with staff, DWA developed the surcharge options and proposals attached to this ruling as Appendix 1.

The essential factors taken into account by the staff are these. According to the large settlement (at 23), Surcharge 2 is estimated to collect \$71.5 million (which is not the capped amount and the capped amount will be treated as Contributions of Aid of Construction (CIAC)). The parties agreed to increase the rate of collection of Surcharge 1 to 20% when the certificate of public convenience and necessity (CPCN) would be issued to make for a smooth transition. Cal Am's fixed equity investment of the project is capped at 27% of the value of the total project costs for the desal plant and the CAW-only facilities. Costs of implementing the securitization plan may be collected through Surcharge 2 in addition to the \$71.5 million for the plant and CAW-only facilities.

The DWA has calculated that letting Surcharge 1 expire naturally and implementing Surcharge 2 thereafter provides the least fluctuation in customer bills, increases the rate payer portion of the Monterey Peninsula Water Supply Project (MPWSP), and decreases the total impact of the project on the rate payer by increasing CIAC. Setting Surcharge 2 at 15% starting July 1, 2014, 30% when

² By this reference that informal ruling is confirmed and memorialized.

Surcharge 1 expires (estimated to be by November 1, 2014), and 45% on January 1, 2015, where it would remain until the desal plant is put into service, accomplishes these goals.

In addition to the MPWSP, rates will increase around the 2nd quarter 2015 for the GRC and around the 3rd quarter for the Water Rate Adjustment Mechanism, assuming a timely processing of the advice letter.

Commission precedence for surcharge collection of construction costs in advance of construction can be found in Decision (D.) 12-06-040 (San Clemente Dam) and D.11-05-002 (Klamath River Dams removal).

This Assigned Commissioner Ruling seeks comments of the Parties by May 12, 2014, and reply comments by May 16, 2014, on the DWA options and proposals set out in Appendix 1

IT IS RULED that Parties are requested to file and serve comments on the Division of Water and Audit's options and proposals contained in Appendix 1 by May 12, 2014, and file and serve reply comments by May 16, 2014.

Dated May 2, 2014, at San Francisco, California.

/s/ MICHAEL R. PEEVEY

Michael R. Peevey
Assigned Commissioner

/s/ GARY WEATHERFORD

Gary Weatherford
Co-Assigned
Administrative Law Judge

Appendix 1

Appendix 1

Annual Revenue requirement for Main, HH, RR and B
No Change

\$50,000,000

Date	Surcharge 1 (%)	Surcharge 1 (\$\$\$s)	Sub total	Surcharge 2 (%)	Surcharge 2 (\$\$\$)	Surcharge 2 Subtotal	Total Surcharge Collections	Effective %
Apr-14	15	625	625				625	15
May-14	15	625	1250				1250	15
Jun-14	15	625	1875				1875	15
Jul-14	15	625	2500				2500	15
Aug-14	15	625	3125				3125	15
Sep-14	15	625	3750				3750	15
Oct-14	15	625	4375				4375	15
Nov-14							4375	0
Dec-14							4375	0
Jan-15							4375	0
Feb-15							4375	0
Mar-15							4375	0
Apr-15				15	\$625	\$625	5000	15
May-15				15	\$625	\$1,250	5625	15
Jun-15				15	\$625	\$1,875	6250	15
Jul-15				30	\$1,250	\$3,125	7500	30
Aug-15				30	\$1,250	\$4,375	8750	30
Sep-15				30	\$1,250	\$5,625	10000	30
Oct-15				30	\$1,250	\$6,875	11250	30
Nov-15				30	\$1,250	\$8,125	12500	30
Dec-15				30	\$1,250	\$9,375	13750	30
Jan-16				45	\$1,875	\$11,250	15625	45
Feb-16				45	\$1,875	\$13,125	17500	45
Mar-16				45	\$1,875	\$15,000	19375	45
Apr-16				45	\$1,875	\$16,875	21250	45
May-16				45	\$1,875	\$18,750	23125	45
Jun-16				45	\$1,875	\$20,625	25000	45
Jul-16				60	\$2,500	\$23,125	27500	60
Aug-16				60	\$2,500	\$25,625	30000	60
Sep-16				60	\$2,500	\$28,125	32500	60
Oct-16				60	\$2,500	\$30,625	35000	60
Nov-16				60	\$2,500	\$33,125	37500	60
Dec-16				60	\$2,500	\$35,625	40000	60
Jan-17				60	\$2,500	\$38,125	42500	60
Feb-17				60	\$2,500	\$40,625	45000	60
Mar-17				60	\$2,500	\$43,125	47500	60
Apr-17				60	\$2,500	\$45,625	50000	60
May-17				60	\$2,500	\$48,125	52500	60
Jun-17				60	\$2,500	\$50,625	55000	60
Jul-17				60	\$2,500	\$53,125	57500	60
Aug-17				60	\$2,500	\$55,625	60000	60
Sep-17				60	\$2,500	\$58,125	62500	60
Oct-17				60	\$2,500	\$60,625	65000	60
Nov-17				60	\$2,500	\$63,125	67500	60
Dec-17				60	\$2,500	\$65,625	70000	60
Jan-18				60	\$2,500	\$68,125	72500	60
Feb-18				60	\$2,500	\$70,625	75000	60
Mar-18				60	\$2,500	\$73,125	77500	60
Apr-18				60	\$2,500	\$75,625	80000	60
May-18				60	\$2,500	\$78,125	82500	60
Jun-18				60	\$2,500	\$80,625	85000	60
Jul-18				60	\$2,500	\$83,125	87500	60
Aug-18				60	\$2,500	\$85,625	90000	60

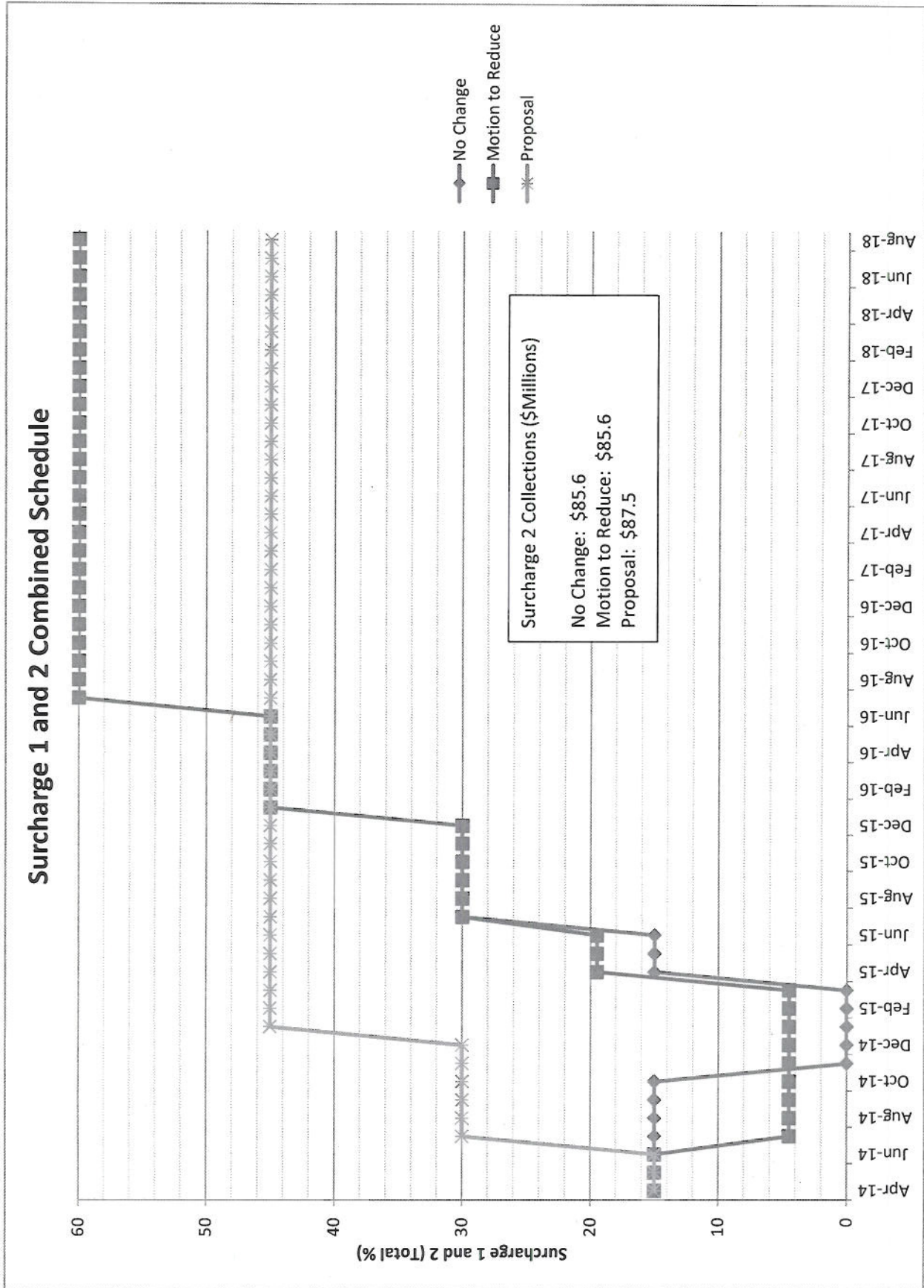
Annual Revenue requirement for Main, HH, RR and B
Motion to Reduce Surcharge 1

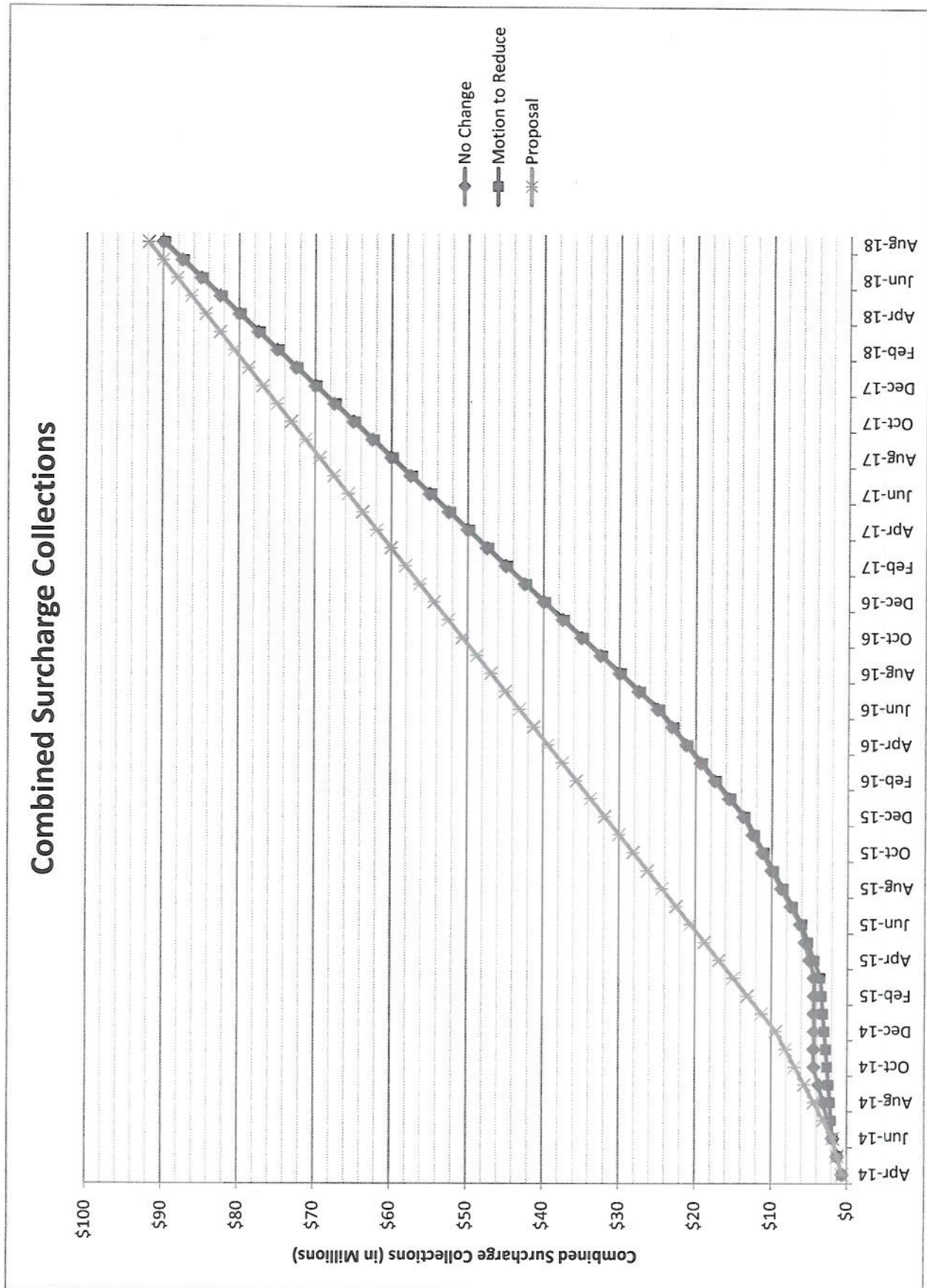
\$50,000,000

Date	Surcharge 1 (%)	Surcharge 1 (\$\$\$)	Sub total	Surcharge 2 (%)	Surcharge 2 (\$\$\$)	Surcharge 2 Subtotal	Total Surcharge Collections	Effective %
Apr-14	15	625	625				625	15
May-14	15	625	1250				1250	15
Jun-14	15	625	1875				1875	15
Jul-14	4.5	187.5	2062.5				2062.5	4.5
Aug-14	4.5	187.5	2250				2250	4.5
Sep-14	4.5	187.5	2437.5				2437.5	4.5
Oct-14	4.5	187.5	2625				2625	4.5
Nov-14	4.5	187.5	2812.5				2812.5	4.5
Dec-14	4.5	187.5	3000				3000	4.5
Jan-15	4.5	187.5	3187.5				3187.5	4.5
Feb-15	4.5	187.5	3375				3375	4.5
Mar-15	4.5	187.5	3562.5				3562.5	4.5
Apr-15	4.5	187.5	3750	15	\$625	\$625	4375	19.5
May-15	4.5	187.5	3937.5	15	\$625	\$1,250	5187.5	19.5
Jun-15	4.5	187.5	4125	15	\$625	\$1,875	6000	19.5
Jul-15				30	\$1,250	\$3,125	7250	30
Aug-15				30	\$1,250	\$4,375	8500	30
Sep-15				30	\$1,250	\$5,625	9750	30
Oct-15				30	\$1,250	\$6,875	11000	30
Nov-15				30	\$1,250	\$8,125	12250	30
Dec-15				30	\$1,250	\$9,375	13500	30
Jan-16				45	\$1,875	\$11,250	15375	45
Feb-16				45	\$1,875	\$13,125	17250	45
Mar-16				45	\$1,875	\$15,000	19125	45
Apr-16				45	\$1,875	\$16,875	21000	45
May-16				45	\$1,875	\$18,750	22875	45
Jun-16				45	\$1,875	\$20,625	24750	45
Jul-16				60	\$2,500	\$23,125	27250	60
Aug-16				60	\$2,500	\$25,625	29750	60
Sep-16				60	\$2,500	\$28,125	32250	60
Oct-16				60	\$2,500	\$30,625	34750	60
Nov-16				60	\$2,500	\$33,125	37250	60
Dec-16				60	\$2,500	\$35,625	39750	60
Jan-17				60	\$2,500	\$38,125	42250	60
Feb-17				60	\$2,500	\$40,625	44750	60
Mar-17				60	\$2,500	\$43,125	47250	60
Apr-17				60	\$2,500	\$45,625	49750	60
May-17				60	\$2,500	\$48,125	52250	60
Jun-17				60	\$2,500	\$50,625	54750	60
Jul-17				60	\$2,500	\$53,125	57250	60
Aug-17				60	\$2,500	\$55,625	59750	60
Sep-17				60	\$2,500	\$58,125	62250	60
Oct-17				60	\$2,500	\$60,625	64750	60
Nov-17				60	\$2,500	\$63,125	67250	60
Dec-17				60	\$2,500	\$65,625	69750	60
Jan-18				60	\$2,500	\$68,125	72250	60
Feb-18				60	\$2,500	\$70,625	74750	60
Mar-18				60	\$2,500	\$73,125	77250	60
Apr-18				60	\$2,500	\$75,625	79750	60
May-18				60	\$2,500	\$78,125	82250	60
Jun-18				60	\$2,500	\$80,625	84750	60
Jul-18				60	\$2,500	\$83,125	87250	60
Aug-18				60	\$2,500	\$85,625	89750	60

Annual Revenue requirement for Main, HH, RR and B \$50,000,000
 Begin Surcharge 2 at 30% when Surcharge 1 Ends and jump to 45% capped

Date	Surcharge 1 (%)	Surcharge 1 (\$\$\$s)	Sub total	Surcharge 2 (%)	Surcharge 2 (\$\$\$)	Surcharge 2 Subtotal	Total Surcharge Collections	Effective %
Apr-14	15	625	625				625	15
May-14	15	625	1250				1250	15
Jun-14	15	625	1875				1875	15
Jul-14	15	625	2500	15	\$625	\$625	3125	30
Aug-14	15	625	3125	15	\$625	\$1,250	4375	30
Sep-14	15	625	3750	15	\$625	\$1,875	5625	30
Oct-14	15	625	4375	15	\$625	\$2,500	6875	30
Nov-14				30	\$1,250	\$3,750	8125	30
Dec-14				30	\$1,250	\$5,000	9375	30
Jan-15				45	\$1,875	\$6,875	11250	45
Feb-15				45	\$1,875	\$8,750	13125	45
Mar-15				45	\$1,875	\$10,625	15000	45
Apr-15				45	\$1,875	\$12,500	16875	45
May-15				45	\$1,875	\$14,375	18750	45
Jun-15				45	\$1,875	\$16,250	20625	45
Jul-15				45	\$1,875	\$18,125	22500	45
Aug-15				45	\$1,875	\$20,000	24375	45
Sep-15				45	\$1,875	\$21,875	26250	45
Oct-15				45	\$1,875	\$23,750	28125	45
Nov-15				45	\$1,875	\$25,625	30000	45
Dec-15				45	\$1,875	\$27,500	31875	45
Jan-16				45	\$1,875	\$29,375	33750	45
Feb-16				45	\$1,875	\$31,250	35625	45
Mar-16				45	\$1,875	\$33,125	37500	45
Apr-16				45	\$1,875	\$35,000	39375	45
May-16				45	\$1,875	\$36,875	41250	45
Jun-16				45	\$1,875	\$38,750	43125	45
Jul-16				45	\$1,875	\$40,625	45000	45
Aug-16				45	\$1,875	\$42,500	46875	45
Sep-16				45	\$1,875	\$44,375	48750	45
Oct-16				45	\$1,875	\$46,250	50625	45
Nov-16				45	\$1,875	\$48,125	52500	45
Dec-16				45	\$1,875	\$50,000	54375	45
Jan-17				45	\$1,875	\$51,875	56250	45
Feb-17				45	\$1,875	\$53,750	58125	45
Mar-17				45	\$1,875	\$55,625	60000	45
Apr-17				45	\$1,875	\$57,500	61875	45
May-17				45	\$1,875	\$59,375	63750	45
Jun-17				45	\$1,875	\$61,250	65625	45
Jul-17				45	\$1,875	\$63,125	67500	45
Aug-17				45	\$1,875	\$65,000	69375	45
Sep-17				45	\$1,875	\$66,875	71250	45
Oct-17				45	\$1,875	\$68,750	73125	45
Nov-17				45	\$1,875	\$70,625	75000	45
Dec-17				45	\$1,875	\$72,500	76875	45
Jan-18				45	\$1,875	\$74,375	78750	45
Feb-18				45	\$1,875	\$76,250	80625	45
Mar-18				45	\$1,875	\$78,125	82500	45
Apr-18				45	\$1,875	\$80,000	84375	45
May-18				45	\$1,875	\$81,875	86250	45
Jun-18				45	\$1,875	\$83,750	88125	45
Jul-18				45	\$1,875	\$85,625	90000	45
Aug-18				45	\$1,875	\$87,500	91875	45





Appendix 2

Excerpt from Joint Motion

(Footnotes deleted)

California-American Water Company (California American Water), Citizens for Public Water, City of Pacific Grove, Coalition of Peninsula Businesses, County of Monterey, Monterey County Water Resources Agency, Monterey Peninsula Regional Water Authority, Monterey Peninsula Water Management District, the Office of Ratepayer Advocates, and Planning and Conservation League Foundation (collectively, the “Settling Parties”) file this joint motion to reduce the Special Request 1 Surcharge (“Surcharge 1”). Specifically, the Settling Parties seek authority for California American Water to reduce the amount of Surcharge 1 from 15% to 4.5% of customer bills. This reduction is reasonable in light of the new Commission schedule for the proposed Monterey Peninsula Water Supply Project (“MPWSP”). The reduction will also benefit ratepayers by avoiding an unnecessary fluctuation in rates and by reducing current bills. Additionally, parties have agreed that California American Water will not seek recovery of any additional costs through Surcharge 1 beyond those requests currently pending before the Commission in A.12-10-003 and A.13-05-017. The Settling Parties request that the Commission act as soon as possible to authorize this agreement and the corresponding reduction in Surcharge 1 in order to maximize the benefit to customers.

II. Legal and Factual Background

In D.03-09-022, the Commission authorized California American Water to track preconstruction costs related to a long-term water supply project in a memorandum account. In D.06-12-040, the Commission authorized California American Water to recover via Surcharge 1 the long-term water supply project costs that it was tracking in that memorandum account. The Commission also approved the Special Request 2 Surcharge (Surcharge 2), which would fund the construction of a water supply solution on a pay-as-you-go basis, but delayed implementation of Surcharge 2 until the issuance of a Certificate of Public Convenience and Necessity (CPCN) for a long-term water supply project.

In D.11-09-039, the Commission authorized California American Water to increase Surcharge 1 to 15%. The increase was approved based on a schedule that provided for

amortization of the approximately \$30 million in preconstruction costs booked in the memorandum account by the end of 2014.

In the current application for the MPWSP, California American Water proposed to continue using Surcharge 1 at the 15% rate to recover preconstruction costs, and asked the Commission to reinstate Surcharge 2. As part of the July 31, 2013 Settlement Agreement, the parties agreed that Surcharge 1 will cease before Surcharge 2 collections begin, allowing for a more gradual ramping up of rates that are directly attributed to the MPWSP. The parties also agreed that the total to be collected under Surcharge 2 will be reduced in order to provide for a smooth transition in rates from the final period under Surcharge 2 to the year 1 revenue requirement of the desalination plant.

III. Justification For Relief

In its application, California American Water proposed a schedule that would provide a Commission decision on the CPCN by February 2013. That schedule was rejected, and an extended procedural schedule was adopted. Most recently, on January 27, 2014, assigned Administrative Law Judge Minkin extended the current schedule for the proceeding to accommodate a delay in the environmental review process. Under the new schedule, a Commission decision on the MPWSP is not expected until the first quarter of 2015. In the meantime, California American Water will continue to recover preconstruction costs through Surcharge 1.

With the current 15% rate, California American Water expects to have recovered the costs through Surcharge 1 by Fall 2014. The extended procedural schedule, however, allows California American Water to be less aggressive in recovery of preconstruction costs and justifies reducing Surcharge 1 to 4.5%. As shown in the attached schedule (Attachment 1), this will still allow California American Water to recover the preconstruction costs in a timely manner and will also smooth rate reductions during the transition from Surcharge 1 to Surcharge 2. Moreover, this reduction will benefit California American Water's Monterey County District customers by reducing current bills. This relief will be helpful for all California American Water customers, but will particularly assist low-income customers facing a variety of increases. Furthermore, the parties have agreed that California American Water will not seek recovery of

any additional costs through Surcharge 1 beyond those requests currently pending before the Commission in A.12-10-003 and A.13-05-017.

IV. Request For Timely Action

The Settling Parties request that the Commission act as soon as possible to authorize the reduction of Surcharge 1. The sooner Surcharge 1 is reduced, the greater the benefit for California American Water's customers. Furthermore, since California American Water is currently on track to recover the existing preconstruction costs by Fall 2014 under the 15% rate, a significant delay would render the issue moot. Timely action on this motion will serve the public interest.

V. Conclusion

Given the delay in the proceeding and the extended period for recovery of preconstruction costs, the Settling Parties' request to reduce Surcharge 1 from 15% to 4.5% of customer bills is justified. California American Water will still be able to recover costs in a timely manner, but customers will benefit in the meantime from a reduced surcharge on their California-American Water Company (California American Water), Citizens for Public Water, City of Pacific Grove, Coalition of Peninsula Businesses, County of Monterey, Monterey County Water Resources Agency, Monterey Peninsula Regional Water Authority, Monterey Peninsula Water Management District, the Office of Ratepayer Advocates, and Planning and Conservation League Foundation (collectively, the Settling Parties) file this joint motion to reduce the Special Request 1 Surcharge (Surcharge 1). Specifically, the Settling Parties seek authority for California American Water to reduce the amount of Surcharge 1 from 15% to 4.5% of customer bills. This reduction is reasonable in light of the new Commission schedule for the proposed Monterey Peninsula Water Supply Project (MPWSP). The reduction will also benefit ratepayers by avoiding an unnecessary fluctuation in rates and by reducing current bills. Additionally, parties have agreed that California American Water will not seek recovery of any additional costs through Surcharge 1 beyond those requests currently pending before the Commission in Application (A.) 12-10-003 and A.13-05-017. The Settling Parties request that the Commission act as soon as possible to authorize this agreement and the corresponding reduction in Surcharge 1 in order to maximize the benefit to customers.

II. Legal And Factual Background

In D.03-09-022, the Commission authorized California American Water to track preconstruction costs related to a long-term water supply project in a memorandum account. In D.06-12-040, the Commission authorized California American Water to recover via Surcharge 1 the long-term water supply project costs that it was tracking in that memorandum account. The Commission also approved the Special Request 2 Surcharge (Surcharge 2), which would fund the construction of a water supply solution on a pay-as-you-go basis, but delayed implementation of Surcharge 2 until the issuance of a Certificate of Public Convenience and Necessity (CPCN) for a long-term water supply project.

In D.11-09-039, the Commission authorized California American Water to increase Surcharge 1 to 15%. The increase was approved based on a schedule that provided for amortization of the approximately \$30 million in preconstruction costs booked in the memorandum account by the end of 2014.

In the current application for the MPWSP, California American Water proposed to continue using Surcharge 1 at the 15% rate to recover preconstruction costs, and asked the Commission to reinstate Surcharge 2. As part of the July 31, 2013 Settlement Agreement, the parties agreed that Surcharge 1 will cease before Surcharge 2 collections begin, allowing for a more gradual ramping up of rates that are directly attributed to the MPWSP. The parties also agreed that the total to be collected under Surcharge 2 will be reduced in order to provide for a smooth transition in rates from the final period under Surcharge 2 to the year 1 revenue requirement of the desalination plant.

III. Justification For Relief

In its application, California American Water proposed a schedule that would provide a Commission decision on the CPCN by February 2013. That schedule was rejected, and an extended procedural schedule was adopted. Most recently, on January 27, 2014, assigned Administrative Law Judge Minkin extended the current schedule for the proceeding to accommodate a delay in the environmental review process. Under the new schedule, a Commission decision on the MPWSP is not expected until the first quarter of 2015. In the meantime, California American Water will continue to recover preconstruction costs through Surcharge 1.

With the current 15% rate, California American Water expects to have recovered the costs through Surcharge 1 by Fall 2014. The extended procedural schedule, however, allows California American Water to be less aggressive in recovery of preconstruction costs and justifies reducing Surcharge 1 to 4.5%. As shown in the attached schedule (Attachment 1), this will still allow California American Water to recover the preconstruction costs in a timely manner and will also smooth rate reductions during the transition from Surcharge 1 to Surcharge 2. Moreover, this reduction will benefit California American Water's Monterey County District customers by reducing current bills. This relief will be helpful for all California American Water customers, but will particularly assist low-income customers facing a variety of increases. Furthermore, the parties have agreed that California American Water will not seek recovery of any additional costs through Surcharge 1 beyond those requests currently pending before the Commission in A.12-10-003 and A.13-05-017.

IV. Request For Timely Action

The Settling Parties request that the Commission act as soon as possible to authorize the reduction of Surcharge 1. The sooner Surcharge 1 is reduced, the greater the benefit for California American Water's customers. Furthermore, since California American Water is currently on track to recover the existing preconstruction costs by Fall 2014 under the 15% rate, a significant delay would render the issue moot. Timely action on this motion will serve the public interest.

V. Conclusion

Given the delay in the proceeding and the extended period for recovery of preconstruction costs, the Settling Parties' request to reduce Surcharge 1 from 15% to 4.5% of customer bills is justified. California American Water will still be able to recover costs in a timely manner, but customers will benefit in the meantime from a reduced surcharge on their bills. The Settling Parties urge the Commission to authorize the reduction of Surcharge 1 as soon as possible in order to provide the greatest benefit to its customers.

(End of Appendix 2)

Appendix 3

Excerpt from Application

(Footnotes deleted)

V. MODIFICATIONS OF EXISTING RATEMAKING MECHANISMS

California American Water is requesting that the Commission: (1) subcategorize the types of costs tracked in the existing memorandum account, (2) reinstitute Surcharge 2 with modifications, (3) adopt a cost cap similar to the one approved in D.10-12-016, and (4) continue the previously authorized ratemaking treatment for the California American Water-only facilities.

A. Memorandum Account

For several years, California American Water has been tracking costs related to a long-term water supply solution for Monterey in a Commission-authorized memorandum account and filing an annual application for review and recovery of the tracked costs. California American Water recovers the reviewed and approved costs through Surcharge 1, which the Commission approved in D.06-12-040. California American Water proposes to continue this process, but to subdivide the various categories of costs. In order to avoid delay, California American Water requests that the Commission issue an interim decision addressing this particular proposal. Subcategory 1A will consist of costs related to the Regional Desalination Project that California American Water incurred before the project's demise, as well as the costs to "unwind" the Regional Desalination Project and related agreements. California American Water proposes to recover these costs through the existing annual application process established in D.08-12-034. California American Water will recover these costs through Surcharge 1A.

Subcategory 1B will consist of costs related to the Monterey Peninsula Water Supply Project, including costs related to a test well and other pre-construction costs. California American Water seeks to use the existing annual review process for review and recovery of the test well and other pre-construction costs related to the Monterey Peninsula Water Supply Project. California American Water will recover these costs through Surcharge 1B.

It is particularly important that the Commission issue an interim decision addressing the ability to track costs related to the test well and recover them in rates. Data from this well will assist with the design of the Monterey Peninsula Water Supply Project, will assess the individual well capacities to determine the final number of intake wells needed, and will help assess the levels of salinity. California American Water seeks to proceed with the test well as soon as possible.

The current estimated cost of the test well is \$5 million. Although California American Water believes that the Commission's earlier decisions authorize it to track and recover costs related to any long-term water supply solution, it is concerned parties may attempt to prevent recovery of the test well and related pre-construction costs as a way to derail the Monterey Peninsula Water Supply Project. Therefore, California American Water requests that the Commission issue an interim decision authorizing California American Water to track the costs for the test well for the Monterey Peninsula Water Supply Project, as well as all other preconstruction costs for the Project, in subcategory B of the memorandum account.

An interim decision will allow California American Water to proceed with these crucial activities and avoid delay. Although California American Water believes this application, along with appendices and supporting testimony, provides sufficient information to rule on its request for interim relief, if after protests and responses to the application are filed the assigned Administrative Law Judge requires more information, California American Water recommends that the parties to this proceeding file concurrent pleadings on the issue, in accordance with the schedule provided below.

B. Surcharge 2

Surcharge 1 provides recovery of preconstruction costs. The Commission approved Surcharge 2 in D.06-12-040 to fund construction costs on a pay-as-you-go basis.²⁷

In D.06-12-040, the Commission authorized California American Water to implement Surcharge 2 immediately after the Commission issued a CPCN for the Coastal Water Project or an alternative long-term supply solution. Initially, the surcharge was to be 15% on customer bills, increasing to 30%, 45% and 60%, respectively, on July 1 and January 1 each year, and was to remain at the 60% level through completion of the approved long-term water supply project.

In D.10-12-016, the Commission found that Surcharge 2 was no longer applicable because the Regional Desalination Project would be financed by the public agencies.²⁹

However, Surcharge 2 is necessary to avoid rate shock and reduces the overall cost of the project to customers. Now that California American Water will be financing and owning the facilities, reinstatement of Surcharge 2, with a few modifications, is appropriate. For example, while Surcharge 2 should still commence immediately after issuance of a CPCN, the surcharge should be 30% initially, increase to 45% and 60% on the subsequent July 1 and January 1, and then remain at the 60% level through completion of the Monterey Peninsula Water Supply Project. Based on the \$260 million capital cost for the 9.0 mgd plant, Surcharge 2 will collect 38% of the capital costs. Based on the \$213 million capital cost for the 5.4 mgd plant, the surcharge will collect 47% of the capital costs. On May 15 of each year after approval, California American Water will file an advice letter to adjust the rate downward if it estimates that the surcharge collection will cover more than those percentages of project costs, effective July 1 of that year. Surcharge 2 should remain in place until the Monterey Peninsula Water Supply Project is in service. California American Water will track the surcharge collections in a memorandum account. Since the surcharge collections will offset costs, those costs should therefore not be included in the capitalized costs and the surcharge collections should not be included as contributions.

C. Desalination Facility Cost Cap

In D.10-12-016, the Commission approved an overall cost cap for the Regional Desalination Project, but provided for review and recovery of reasonable cost above the cap, upon a showing that these costs were the result of extraordinary circumstances and subject to a heightened level of scrutiny. California American Water requests that the Commission take the same approach to a cost cap for the Monterey Peninsula Water Supply Project. This would create an incentive for California American Water to manage the Project responsibly, since the Commission could easily disallow unreasonable costs, but would avoid unfairly penalizing California American Water for increased costs beyond its control. Although California American Water is confident that its cost estimates are accurate based on the information currently available, a number of factors beyond California American Water's control could still affect the cost estimate, including escalating costs of labor and materials, actions mandated by other

regulatory agencies, and other project unknowns. California American Water requests that the Commission adopt a \$281.2 cost cap for the 9.0 mgd facility and a \$227.1 cost cap for the 5.4 mgd facility. The cost caps include the estimated capital expenditures, capitalized operating expenses, and allowance for funds used during construction (“AFUDC”).

D. California American Water-Only Facilities

In D.10-12-016, the Commission approved with minor modification to the requested interest rate, the exact request made by the settling parties with respect to the California American Water-only facilities. The Commission established a \$106.875 cost cap for the California American Water facilities, with recovery of costs above the cap upon a showing of extraordinary circumstances and subject to heightened scrutiny. The Commission approved treatment of the California American Water-only facilities as used and useful as soon as they are constructed, even if the Regional Desalination Project was delayed. With the exception of the Transfer Pipeline, California American Water was to record the total cost of the California American Water-only facilities, subject to the capital cost cap and AFUDC calculation, that are completed and used to provide service to customers in its Utility Plant In Service (“UPIS”) Account and the total costs of the projects that are not providing service to customers in the Construction Work in Progress (“CWIP”) Account. Under D.10-12-016, the ratebase for the California American Water-only facilities was to be calculated by determining the sum of UPIS and CWIP, less any grant funds and less any accumulated depreciation.

The Commission authorized California American Water to file a Tier 2 advice letter on May 15 and November 15 each year to include all prudently expended costs related to construction of the California American Water-only facilities into rate base as either CWIP or UPIS, with the increase in January 1, or July 1 regardless of the status of the review. The Commission authorized California American Water to earn AFUDC on all project costs until they were in ratebase and found that it was appropriate to adopt an initial AFUDC rate that is representative of current rates, and allow this rate to be trued-up to reflect actual carrying costs.

California American Water requests that the Commission adopt the same treatment for the California American Water-only facilities in this proceeding that it approved in D.10-12-016, with clarifications to the process set forth in the Direct Testimony of David P. Stephenson.

Generally, however, since the California American Water-only facilities will be the same as the Commission approved in D.10-12-016, there is no reason to change the ratemaking treatment.

(End of Appendix 3)